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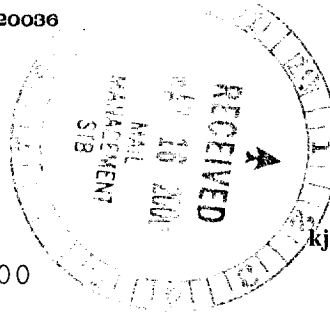
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May 16, 2000

VIA HAND DELIVERY

The Hon. Vernon A. Williams
Secretary
Surface Transportation Board
Case Control Unit
Attn: STB Ex Parte No. 582
1925 K Street, N.W.
Washington, D.C. 20423-0001

Office of the Secretary

MAY 16 2000

Part of
Public Record

Re: Ex Parte No. 582 (Sub No. 1), Major Rail
Consolidation Procedures

Dear Secretary Williams:

Enclosed for filing in the above-referenced proceeding are the original and 25 copies of the Comments of the State of New York. Also enclosed is a 3.5-inch diskette containing the text of this letter and the enclosed Comments in WordPerfect 8.0 format.

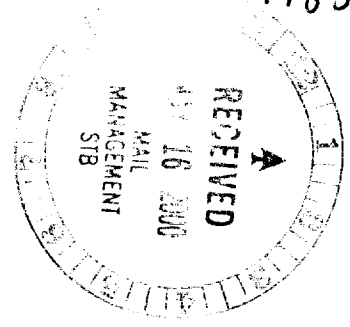
Please acknowledge receipt of the enclosed filing by stamping and returning to our messenger the enclosed duplicate of this letter.

Sincerely,

Kelvin J. Dowd

KJD/cbh
Enclosures

198586



BEFORE THE
SURFACE TRANSPORTATION BOARD

In The Matter Of:

MAJOR RAIL CONSOLIDATION
PROCEDURES

Ex Parte No. 582 (Sub-No. 1)

FILED
Office of the Secretary

MAY 16 2000

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Public Record

COMMENTS OF THE
STATE OF NEW YORK

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Dated: May 16, 2000

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BEFORE THE
SURFACE TRANSPORTATION BOARD

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In The Matter Of:)	
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MAJOR RAIL CONSOLIDATION)	Ex Parte No. 582 (Sub-No. 1)
PROCEDURES)	
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COMMENTS OF THE
STATE OF NEW YORK

The State of New York, acting by and through the New York State Department of Transportation ("New York"), submits its Comments in response to the Advance Notice of Proposed Rulemaking ("Notice") served in this proceeding on March 31, 2000.

IDENTITY AND INTEREST

New York is a sovereign state, having entered the Union through ratification of the Constitution of the United States on July 26, 1788. The New York State Department of Transportation (NYSDOT) is the executive department charged with responsibility for the supervision and administration of state policies and interests with respect to transportation within or affecting New York, including rail transportation.

New York has a long and storied history of commitment to the development and promotion of a sound, efficient and economical surface transportation system. In particular, New York has been in the forefront of public investment in rail facilities, having dedicated nearly \$1 billion in rail infrastructure capital over the past twenty-five years. In addition to the railroads operating within the state, New York's public investments have been directed to the benefit of shippers, ports, passenger rail users, and the communities affected by them. That commitment continues in the present day, with over \$80 million in direct investment and tax-related reforms planned for rail projects and related facilities over the next five years.

In previous presentations before the Board, New York has detailed the evolution of rail freight service in the state and the manner in which shippers, communities and other transportation constituencies gradually became dependent on a single carrier -- Conrail -- for all of their rail service needs. See, e.g., Finance Docket No. 33388, CSX Corporation, Et Al., Control and Operating Leases/Agreements -- Conrail Inc., Et Al., Comments of the State of New York, October 21, 1997, V.S. Utermark at 2-7. More recently, in an earlier phase of this proceeding, NYSDOT Assistant Commissioner John F. Guinan summarized the consequences of the rail industry's steady march

toward consolidation for the state and the rail customers and smaller carriers located within its borders. See Ex Parte No. 582, Public Views On Major Rail Consolidations, Comments of the State of New York, February 29, 2000, V.S. Guinan at 6-8. He further explained how the concerns of these important constituents were given voice through New York's comments and petitions in Finance Docket No. 33388, supra, eventually leading to a series of conditions being imposed on the acquisition and division of Conrail through Board directives and negotiations with the Applicant carriers. Id., at 8-9. Though the implementation of these remedial measures has met with mixed success, a subject to be addressed further in upcoming oversight proceedings in Finance Docket No. 33388 (Sub-Nos. 90 and 91) (see id., at 10-13), New York's historic activism in matters concerning the structure, health and future of the rail transportation industry in the Northeast establishes its interest in the serious policy issues to be addressed in this docket.

SUMMARY OF POSITION

As Mr. Guinan testified in his February 29, 2000 Verified Statement, New York agrees that the time is ripe for a re-evaluation of the Board's merger review guidelines, policies and related regulations. Common sense counsels that policies developed and rules crafted in eras marked by a multiplicity of

Class I railroads with substantial system and service overlaps cannot be counted on to continue to serve the public interest effectively after the rail map has been dramatically redrawn to show only a handful of mega-carriers, generally linked end-to-end, with an extensive system of dependent shortlines and regional railroads serving as origin and termination carriers for branch line traffic. New York commends the Board for recognizing the need for reform of its rail merger rules and policies, and for soliciting the views of New York and other states, as well as shippers, carriers and the myriad other affected interests prior to issuing any new, proposed rules.

New York's general suggestions regarding appropriate changes to the Board's rail merger policies and guidelines are set forth in the following section of these Comments. New York intends to participate in further phases of this proceeding, and will comment specifically on formal rules changes offered by the Board in the Notice of Proposed Rulemaking expected in October, 2000, once it is served. By reference to specific issue areas delineated in the March 31 Notice, however, New York's preliminary views may be summarized as follows:

1. The Board should look for opportunities to promote and expand rail-to-rail competition through exercise of its merger conditioning authority.
2. In considering merger Safety Integration Plans, the Board should require Applicants to address future coordination of freight operations with commuter and inter-city passenger service.
3. The Board should adopt rules requiring merger Applicants to submit detailed service implementation plans, and subject such plans to close scrutiny to ensure that the scope and quality of service is not degraded post-merger.
4. The Board should develop guidelines to protect the interests of shortlines and regional railroads affected by proposed mergers, including the elimination of anti-competitive interchange barriers.
5. The new merger guidelines should include heightened scrutiny of claimed merger benefits, and measures to ensure that customers and communities do not bear the burdens of overly-optimistic expectations or operating cost increases resulting from transition problems.

Finally, New York believes that the Board must ensure that it has the staffing and analytical resources necessary to effectively administer its new guidelines and the public protections that properly should be among their core features.

COMMENTS OF
THE STATE OF NEW YORK

I. THE BOARD'S NEW GUIDELINES SHOULD PROMOTE
AND ENHANCE RAILROAD COMPETITION

In the Notice, the Board observed that "the time has come to consider whether we should alter our rail merger policy to place a greater emphasis on enhancing, rather than simply preserving, competition." Notice at 7. New York submits that such consideration indeed is called for, and that upon reflection on the current state of the industry and analysis of the relevant policy interests, the Board should adopt proactive guidelines that call for the exercise of the agency's conditions authority to promote new competition through the rail merger review process.

In response to the proposal by CSXT and Norfolk Southern to acquire and divide Conrail, New York petitioned the Board, inter alia, for an order requiring the establishment of competitive, dual carrier rail service East of the Hudson River, a market which under the Applicants' proposal would have been the exclusive domain of CSXT. The petition was grounded on considerations of current, relative regional competition -- shippers West of the Hudson were to benefit from voluntary competition between CSXT and Norfolk Southern through their creation of a Shared Assets Area -- as well as the larger, policy

question of whether the rail industry had become so concentrated that affirmative action was needed to restore competition that historically had existed but had been lost long before the transaction under consideration was proposed. Acknowledging that what was at issue had to be considered "new competition," the Board granted the relief sought by New York:

We have carefully balanced the needs of the competing parties here, and strongly believe that we must forcefully use this opportunity to restore a modicum of the competition that was lost in the financial crisis that led to the formation of Conrail.

...

Therefore, we will impose a condition requiring CSX to negotiate an agreement with [Canadian Pacific Railway] to permit either haulage rights, not restricted as to commodity or geographic scope, or similarly unrestricted trackage rights, over the east-of-the-Hudson line... .

Finance Docket No. 33388, Decision served July 23, 1998 at 83.

The ultimate outcome of the Board's action was the establishment of competitive, dual carrier service via trackage rights, with both CSXT and Canadian Pacific serving shippers and terminals East of the Hudson River and in New York City.

New York submits that the Board's East-of-Hudson condition in Finance Docket No. 33388 should serve as an instructive starting point for a revision of the Board's merger review policies vis-a-vis the promotion of new competition. Given the current degree of market power concentration

characterizing the major railroad network, any new combination would present multiple examples of terminals, regions or even individual shipping points that in the past enjoyed a measure of effective rail competition. The Board's new guidelines should provide that upon such a showing by an affected shipper, community or other relevant constituent, conditions would be imposed to reopen the area in question to competitive rail service, either through trackage rights in favor of a connecting carrier (including a shortline) or -- depending upon the location and available rail infrastructure -- haulage or reciprocal switching on reasonable, non-discriminatory terms.

II. THE BOARD SHOULD ADOPT AN EXPANSIVE
APPROACH TO RAIL SAFETY IN DEVELOPING
NEW RAIL MERGER GUIDELINES

New York respects the Board's view that rail safety issues raised by a prospective merger or other consolidation are best addressed on a case-by-case basis in the context of environmental impact review and the Safety Integration Plans that merger Applicants already are required to develop in cooperation with the Federal Railway Administration. See Notice at 6. New York does not intend to advocate new or revised rules vis-a-vis Board consideration of rail safety concerns arising from proposed mergers. Consistent with its position espoused in Finance Docket

No. 33388 regarding passenger-freight relations and the rights of states under contracts undertaken in consideration of public investment in railroad infrastructure, however, New York respectfully urges the Board to re-affirm its commitment to use its conditions authority to protect publicly-supported passenger rail interests. See id., Comments of the State of New York, October 21, 1997, V.S. Utermark at 8-20.

Though not generally considered within the rubric of rail safety issues raised by a proposed merger, freight carriers' respect for and adherence to state policies and priorities regarding the development and expansion of commuter and inter-city passenger service clearly contributes to the maintenance of a "safe and efficient rail transportation system... ." See 49 U.S.C. Section 10101(3). A robust passenger rail system promotes energy conservation as well as public safety, benefits closely tied to reduced dependence on automobiles as a means of personal transportation. New York's commitment to passenger rail technology, research and development is well-documented, and is a cornerstone of the state's transportation policy goals for the 21st Century. As Mr. Guinan recently confirmed, New York is prepared to make the investments necessary to pursue and achieve these goals, as it has done throughout its history. See Ex Parte No. 582, supra, Comments of

the State of New York, February 29, 2000, V.S. Guinan at 6, 16. In the long run, however, these efforts can only succeed if agencies such as the Board, with plenary authority over the freight railroads that co-exist and often share facilities with commuter and passenger operations, also act to protect the public's investments.

III. THE BOARD'S REVISED MERGER GUIDELINES SHOULD AIM TO SAFEGUARD RAIL SERVICE QUALITY

New York shares the view that a greater emphasis on before-the-fact controls designed to avoid post-merger service disruptions and deteriorated service quality should be a central component of any new rail merger policy guidelines developed by the Board. See Notice at 6. In that regard, New York supports the adoption of rules requiring merger Applicants to prepare, file and be prepared to defend formal rail service impact or implementation plans as part of the overall transaction approval process. Once accepted or approved by the Board at the conclusion of the review proceeding, the specific elements of such a plan -- including representations as to intended service levels, routes, equipment and resource allocations, etc. -- should be imposed by the Board as conditions of approval, enforceable by agency order through subsequent, post-transaction oversight proceedings. In evaluating potential service impacts,

in turn, the Board's new guidelines should include considerations of both scope and quality.

The demonstrated dependency of smaller communities and shippers on adequate rail service to support growth opportunities highlights the need for scrutiny of the likely effects of a proposed transaction on the scope of services that will be available from the surviving entity. Experience shows that when capacity gets tight, rural areas and branch line shippers and terminals are at risk of resource rationing and service curtailments. In formulating the rules for the preparation and submission of service impact plans, the Board should include a requirement that merger Applicants address the provisions to be made for preserving a full range of service options for smaller shippers and branch line communities, both under optimum post-merger conditions and in the event that unforeseen - though not unforeseeable - transition difficulties stretch capacity and constrain resources. The adequacy of existing infrastructure and Applicants' plans for the design and financing of infrastructure expansions, should they be necessary to maintain pre-merger service levels, also should be mandatory components of the analysis.

In addition to the preservation or expansion of the scope of pre-transaction rail service, the Board's new guidelines

should require evidence of steps to be taken and resources to be committed by Applicants to safeguard the quality of service to be offered, including train frequencies, transit times, railcar and locomotive supplies, enhanced use of information technology (particularly in communications with shortline connections), yard schedules, mine or terminal permit systems, and claims resolution. As Mr. Guinan testified in February, a coordinated survey of New York shippers and communities undertaken following consummation of the Conrail acquisition found widespread service inconsistencies, capacity constraints, and unexpected costs for railcar delays, demurrage and other service-related problems. Adverse effects included manufacturing shift curtailments, utility fuel stockpile shortages, and an increase (rather than the expected decrease) in motor freight traffic as shipments were diverted away from rail. See Ex Parte No. 582, supra, Comments of the State of New York, February 29, 2000, V.S. Guinan at 9-10. These problems mirrored those experienced by other Eastern shippers, ports and communities, many of which still await resolution and a return to service levels prevailing prior to the Conrail "split date." New York submits that the range of service deficiencies that have characterized recent mergers -- particularly the Conrail transaction -- can serve as an outline

for the quality-focused components of a new service impact statement requirement.

IV. THE BOARD SHOULD ADOPT GUIDELINES THAT AFFIRMATIVELY PROMOTE THE INTERESTS OF SHORTLINES AND REGIONAL RAILROADS

In Finance Docket No. 33388, the Board responded affirmatively to the petition of the Livonia, Avon & Lakeville Railroad (LAL), a Class III carrier based in Rochester, NY, for relief from an historic interchange barrier that prevented its establishment of a direct connection with a neighboring regional carrier and, thus, limited the scope of its marketing opportunities and the service that it was able to offer to its existing shippers. Though the Board noted that LAL's petition "might appear to be unrelated to any harm caused by [the Conrail] transaction," it nonetheless acknowledged the stated preferences and interests of LAL's customers as legitimate concerns to be served, and directed CSXT to negotiate with LAL for removal of the barrier. See Finance Docket No. 33388, Decision served July 23, 1998 at 102-03.

The public benefits of a vibrant and efficient national network of shortlines and regional railroads have been well-documented, and are universally acknowledged. As Class I carriers have moved to consolidate their systems and focus their marketing and operational strategies on their core, trunk line

routes, smaller regional carriers have stepped into the breach and preserved rail service over branch lines whose traffic volumes -- while critically important to shippers and local businesses -- cannot compete with unit train utility coal and other large bulk commodity accounts. At the same time, shortlines remain dependent on the major carriers in many instances, for access to yards, interchange tracks and line-haul transportation connections. Where the larger carriers impose restrictions on this access, particularly access to alternate railroads and routes, shipper choices are curtailed and the shortlines' growth and revenue opportunities are artificially constrained. Likewise, where the quality of service or adequacy of equipment supply offered by the Class I's deteriorates, or where single-line connections become three carrier hauls as shortlines try to maintain routing options, traffic previously handled by the smaller carriers diverts to motor carriage, often permanently, with a concomitant, negative impact on the carriers' financial health. In New York, for example, shortlines reported revenue losses of as much as 30-40% in the wake of diversions attributable to equipment and service shortfalls resulting from problems experienced by CSXT and Norfolk Southern in the course of their implementation of the Conrail division.

New York submits that the Board should adopt guidelines to address each of the foregoing concerns, in the context of a revised rail merger policy statement. In the case of artificial interchange barriers in the nature of that to which LAL formerly was subject, New York proposes that the Board establish a presumption in favor of the removal of any so-called "paper barriers" to which a merger Applicant is a party, as a condition of approval of the merger. The condition should be imposed at the request of the affected shortline or one of its customers, and the presumption should be rebuttable only by proof either that the barrier serves a pro-competitive purpose, or is part of a legitimate, alternative financing arrangement that only assures the Class I party the actual value of the lines leased or acquired by the shortline.

V. THE BOARD SHOULD ADOPT A POLICY OF
CLOSER SCRUTINY OF CLAIMED MERGER BENEFITS

A consistent pattern that emerges from an objective review of the post-transaction records of recent rail mergers is the often wide disparity between claims made by the Applicants regarding benefits, efficiencies and cost savings expected to flow from their transactions, and the reality of their post-merger performance. The consequences for shippers and affected communities are well-documented and frequently dramatic: a

deterioration of service quality accompanied by rising costs, threatened losses of service to marginal areas, neglect of markets not considered critical to the carriers' core business, and a rationing of limited capacity resulting from the confluence of operational dysfunction and a lack of private investment in infrastructure. To be sure, not all merger-related dislocations were predictable or could have been averted through closer agency scrutiny. However, with only the Applicants' views of synergies and prospective efficiencies before the Board, and with the agency apparently deferential to the claims and estimates of "those who run the railroads," past merger proceedings seem to have painted scenarios where success was assumed, and the only consequences of an error in judgment or implementation would be negative. Simply put, "what if?" is not a question that has tended to characterize the Board's review of past rail merger proposals.

New York applauds the Board's stated willingness to "be more critical and skeptical" of future claims of public interest benefits resulting from new rail mergers or consolidations. See Notice at 9. In addition to more aggressive scrutiny of railroad claims before the fact, however, New York believes that the Board's revised guidelines should provide protections for shippers and communities from prospective economic burdens associated with the recovery of acquisition premiums or higher

rail operating costs resulting from the carriers' failure to realize efficiencies or other claimed merger benefits. The importance of this reform is underscored by the Board's own recent finding that as presently structured and interpreted, standard railroad accounting rules allow carriers to treat the costs of merger-related service crises as ordinary expenses, which presumably can be reflected and recovered through rate increases on captive traffic. See Finance Docket No. 33726, Western Coal Traffic League v. Union Pacific Railroad Company, Decision served May 12, 2000.

At a minimum, the Board's new guidelines should include the following:

1. Applicants should be required to address foreseeable contingencies in their proposed operating plans, and disclose the margins of error (if any) incorporated in any estimates of costs or savings.
2. Board consideration of the impact of a transaction on the carriers' fixed charges under 49 U.S.C. Section 11324(b)(3) should include specific analysis of the carriers' ability to attract adequate capital to upgrade or expand infrastructure to cope with traffic increases or service problems, and the associated costs.

3. Specific conditions should be adopted to preclude carriers from transferring the burdens of merger-related cost overruns or acquisition premiums to shippers or public agencies by including such costs in the carriers' standard accounts used for regulatory purposes.
4. Representations in merger-related operating plans should be reviewed and approved by the Board under a reasonableness standard, then imposed as enforceable conditions should the transaction win final approval.

CONCLUSION

As the Board acknowledged in its Notice, the rail mergers and consolidations that have occurred over the past decade have so changed the North American rail map that continued reliance on merger policy guidelines crafted in and for a different era would threaten the ability of the Board to protect and promote the public interest in efficient, economic and competitive railroad transportation. The challenges that any new merger or consolidation proposals would pose for states, shippers, smaller railroads and other constituencies compel the consideration of meaningful reforms and new rules to assist the Board in discharging its statutory oversight responsibilities. New York commends the proposals included in these Comments to the Board's favorable consideration, and urges that they be adopted.

Respectfully submitted,


THE STATE OF NEW YORK,
ACTING BY AND THROUGH THE
NEW YORK STATE DEPARTMENT OF
TRANSPORTATION

OF COUNSEL:

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Dated: May 16, 2000

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Attorneys & Practitioners

CERTIFICATE OF SERVICE

I hereby certify that on this 16th day of May, 2000, I caused a copy of the foregoing Comments to be served on all persons designated as a Party of Record or Member of Congress in the Board's decisions in this proceeding served April 28 and May 10, 2000, by first-class United States Mail.

A handwritten signature in black ink, appearing to read 'Kelvin J. Dowd', written over a horizontal line.

Kelvin J. Dowd